The Real Estate TRENDS

MAY 31
1957

Volume XXVI

A concise monthly digest of real estate and construction fundamentals and trends . . . A part of the complete service known as the Real Estate Analyst Reports

Number 22

REAL ESTATE ECONOMISTS, APPRAISERS AND COUNSELORS

BY far the most startling development during the past month has been the rather sharp drop in real estate activity. In the April 30, 1957, Real Estate Trends Bulletin it was pointed out that real estate activity, for the first time in more than 13 years, had fallen below the long-term normal, and that in the past when this had happened it had generally indicated the beginning of a long period of readjustment in the real estate field. The new figure shown in this report is now 6.0% below normal, a drop of considerable proportions. This is shown on the chart on page 227.

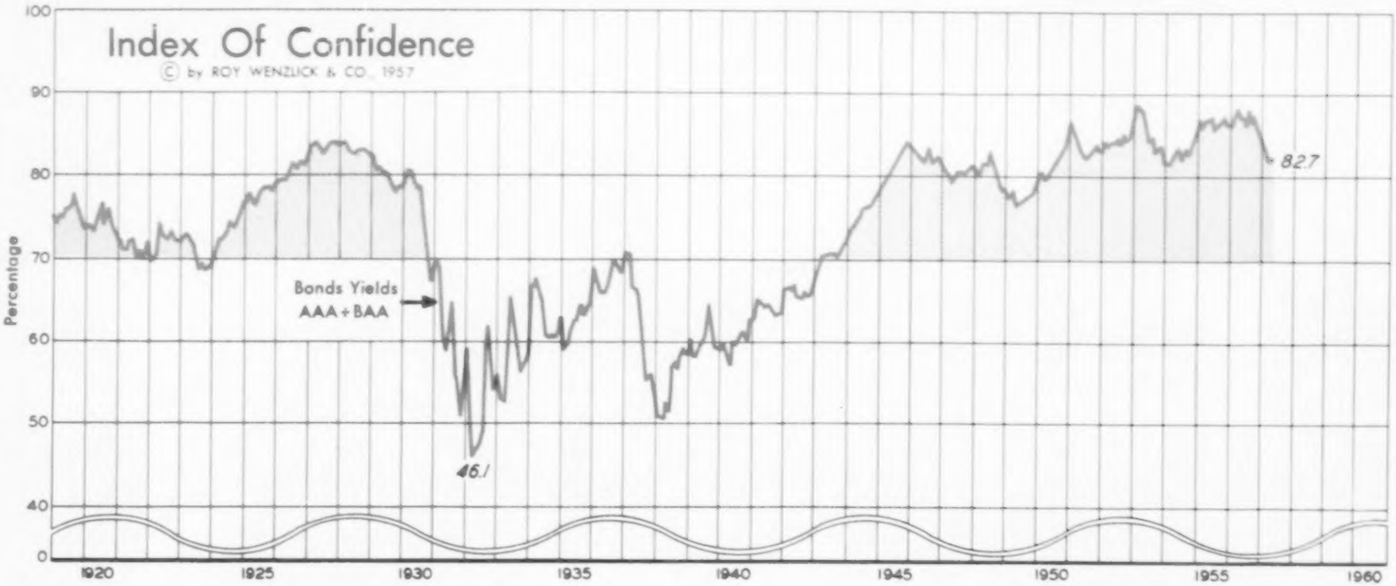
Undoubtedly a portion of the cause for this drop is the drop in new construction. Fewer houses have been finished and put on the market and, therefore, fewer have been sold. Since this has occurred at a time when money was tight for financing existing properties, transfers have been shrinking. A check we have made of the drop in real estate activity at the end of the preceding real estate boom (the one ending in 1929) has shown, however, that the same conditions existed then. Real estate transfers dropped, but at the same time new construction dropped and money was tight.

It is still too early to say definitely that the biggest real estate boom we have ever had has now ended, and that for a longer or shorter time in the future we will be in a period of readjustment. Should this prove to be the case, the big question remaining is whether the adjustment will be mild or drastic.

It seems probable that should this readjustment ensue, it will not be of the type we experienced in the 1930's. The general economy of the United States, we believe, is in a sounder condition than it was in the late 1920's. This should prove stimulating to real estate and construction, preventing the type of drastic drops which we experienced then. New construction at the end of the boom of the 1920's fell to a level less than 10% of that at the peak.

The two weakest portions of the economy at the present time seem to be the real estate field and the automobile field. Many other sections of the economy are still setting new records.

The monthly-payoff mortgage, we believe, will be an element of strength during any readjustment period we might have. In preceding real estate adjustments, mortgages made for 3 or 5 years came due, and often could not be refinanced, bringing on foreclosures which would otherwise not have occurred. These foreclosures threw properties on a disinterested market, further depressing values.



The index of confidence, which is shown above, is still remarkably high, higher than it was in 1929 and 1930, when the real estate situation collapsed before. This index of confidence is prepared on the basis of a study made many years ago by General Leonard P. Ayres. The yield of the very best bonds is divided by the yield of second-rate bonds. The fundamental theory behind this index is that when confidence drops, the investing public will pay a higher price in relation to income for the best type bond than it will for a second-rate bond. When confidence is very high, however, there is relatively little difference in the prices the public will pay for the highest grade and the second grade.

It will be noticed on this chart that in the spring of 1953, second-rate bonds were selling for more than 88% of the price of first grade bonds. At the bottom of the depression, however, second-rate bonds brought only 46% of the price of first grade bonds. At the present time they are bringing approximately 83%.

While this chart is encouraging, it is not con-

(cont. on page 225)

(cont. from page 224)
clusive, in that it indicated a high degree of confidence even as late as 6 months after the beginning of the stock market collapse in 1929 and 1930. Real estate activity dropped more than a year before the index of confidence, and it may be that the same thing is happening again today.

The chart below shows the way various interest rates have varied since the beginning of 1952. Ninety-day Treasury bills, shown by the blue dashed line at the bottom of this chart, probably come fairly close to pure interest. These bills hit a low spot about the middle of 1954, selling for only slightly more than one-half of 1% interest. In contrast, at the beginning of 1957, they were bringing considerably more than 3%. They have dropped since to around 3%, but are still relatively high in comparison with the past.

Long-term Government bonds are running better than 3-1/3%, high-grade municipals slightly better than $3\frac{1}{2}\%$, first-class corporation bonds are paying almost 3-3/4%, while in 12 cities the average recorded mortgage interest rate is slightly better than 5.5%, as can be seen on the table at the top of page 226. It will be noticed on the chart below that mortgage interest rates have risen by almost $\frac{1}{2}\%$ since the end of 1955.

AVERAGE INTEREST RATE OF RECORDED MORTGAGES IN 12 MAJOR CITIES OF THE UNITED STATES

Jan.	'54	5.187%	Jan.	'56	5.105%	Sept.	'56	5.183%
Apr.	'54	5.173	Feb.	'56	5.177	Oct.	'56	5.229
July	'54	5.089	Mar.	'56	5.212	Nov.	'56	5.221
Oct.	'54	5.092	Apr.	'56	5.157	Dec.	'56	5.273
			May	'56	5.158			
Jan.	'55	5.045	June	'56	5.155	Jan.	'57	5.363
Apr.	'55	5.079				Feb.	'57	5.478
July	'55	5.050	July	'56	5.141	Mar.	'57	5.459
Oct.	'55	5.055	Aug.	'56	5.190	Apr.	'57	5.507

These rates are taken from mortgage recordings, which lag actual commitments by a period of time. It should also be kept in mind that the figures of last year are recorded rates which do not include the discounts which were being paid and which were greater at that time than they are now. Were it possible to make these adjustments, the chart would show an increase in interest rates considerably greater than that shown.

(cont. on page 228)

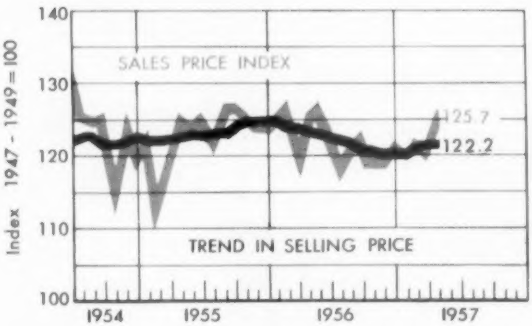
Real Estate Sales Price Comparisons

With preceding month

0.0%

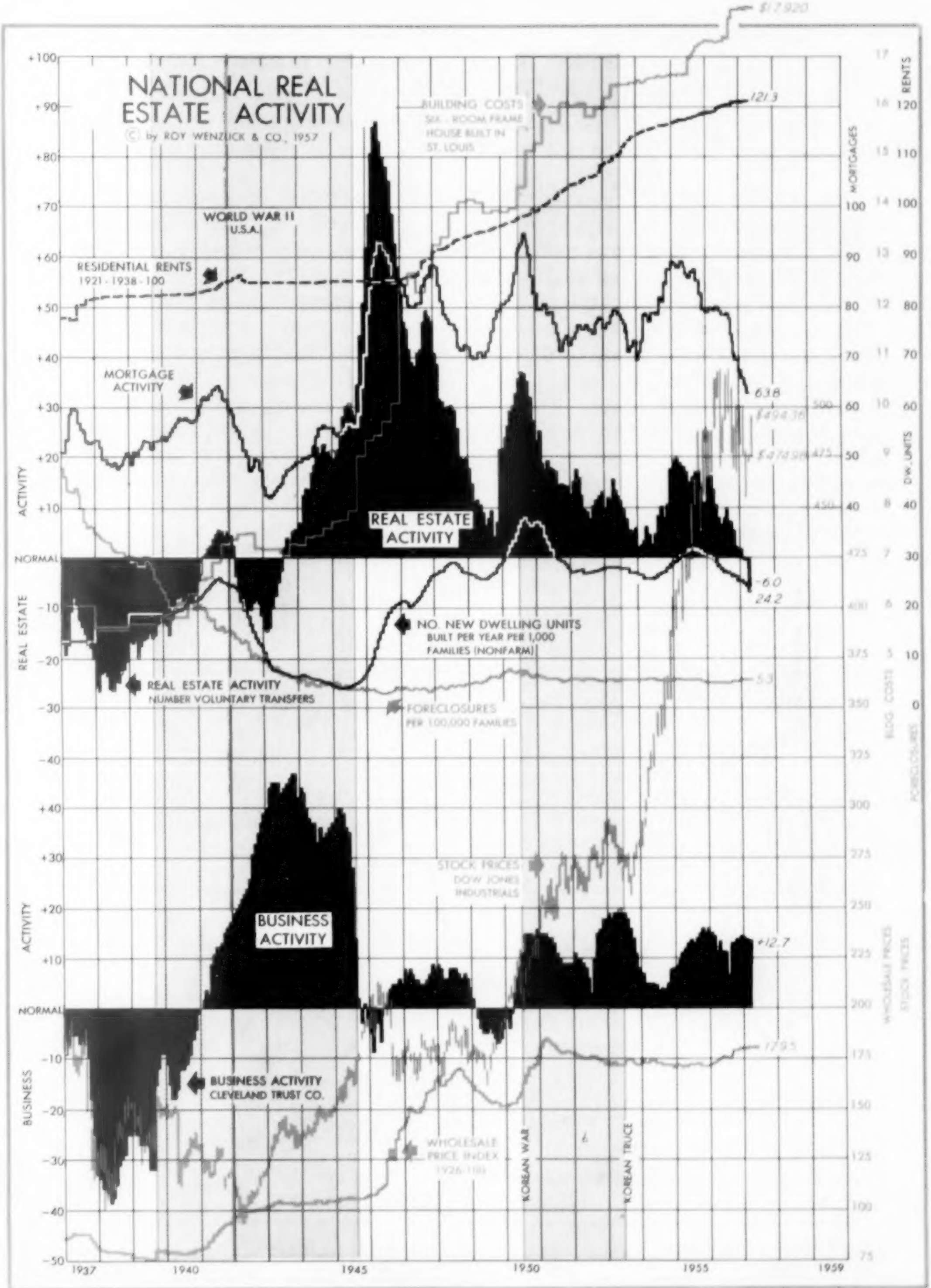
With same month preceding year

-1.6%



Date	Trend in selling price	Probable selling price of a house that sold for $12,000 in 1947-49 period	Date	Trend in selling price	Probable selling price of a house that sold for $12,000 in 1947-49 period
1947-49	100.0	$12,000	Oct. '48	104.5	$12,540
1913	40.1	4,812	Oct. '53	119.7	14,360
1918	34.1	4,092	Oct. '54	122.3	14,680
Mar. '29	73.9	8,868	Jan. '55	122.9	14,750
May '32	34.8	4,176	May '55	123.5	14,820
			Oct. '55	125.1	15,010
Apr. '34	44.8	5,376	Jan. '56	125.3	15,035
July '37	40.1	4,812	May '56	123.5	14,820
			Oct. '56	121.9	14,630
Apr. '38	42.8	5,136	Dec. '56	121.9	14,630
Mar. '41	40.1	4,812	Jan. '57	122.1	14,650
			Feb. '57	122.2	14,665
			Mar. '57	122.2	14,665
			Apr. '57	122.2*	14,665*

*Preliminary.


NATIONAL REAL ESTATE ACTIVITY
© by ROY WENZLICK & CO., 1957
WORLD WAR II U.S.A.
RESIDENTIAL RENTS 1921-1938-100
MORTGAGE ACTIVITY
BUILDING COSTS SIX-ROOM FRAME HOUSE BUILT IN ST. LOUIS
REAL ESTATE ACTIVITY
NO. NEW DWELLING UNITS BUILT PER YEAR PER 1,000 FAMILIES (NONFARM)
REAL ESTATE ACTIVITY NUMBER VOLUNTARY TRANSFERS
FORECLOSURES PER 100,000 FAMILIES
STOCK PRICES DOW JONES INDUSTRIALS
BUSINESS ACTIVITY
BUSINESS ACTIVITY CLEVELAND TRUST CO.
WHOLESALE PRICE INDEX 1926-100
KOREAN WAR
KOREAN TRUCE
REAL ESTATE ACTIVITY
BUSINESS ACTIVITY
NORMAL
MORTGAGES
RENTS
DW. UNITS
BLDG. COSTS
FORECLOSURES
WHOLESALE PRICES
STOCK PRICES
$17,920
121.3
63.8
$494.36
$478.98
-6.0
24.2
5.3
+12.7
179.5
1937
1940
1945
1950
1955
1959

(cont. from page 226)

In spite of the slight drop in pure interest which is being shown on the chart on 90-day Treasury bills, the probability is that the average interest rate of mortgages recorded as shown on this chart will continue to creep up.

The selling price of existing single-family residences showed considerable strength last month in comparison with the gradually dropping price we experienced during 1956. It has been pointed out a number of times in our reports that over a period of years selling prices of existing properties tend to follow replacement cost new, and if construction costs advance, there is a strong probability that existing properties will also advance in price. The only time when this would not be true would be a period in which residential vacancy is high, in which case the surplus of units on the market would prevent any rise in price due to higher replacement costs. The actual surplus of vacant units, however, has been dropping. Figures are available by quarters for the United States on residential vacancy since the second quarter of 1955, and during the past 6 months these figures show that there has been considerable absorption of vacant units. If we continue to absorb vacancies, it will have a very strong stabilizing effect on the values of existing properties, and with construction costs still rising, we can expect the values of existing properties to develop an upward drift.

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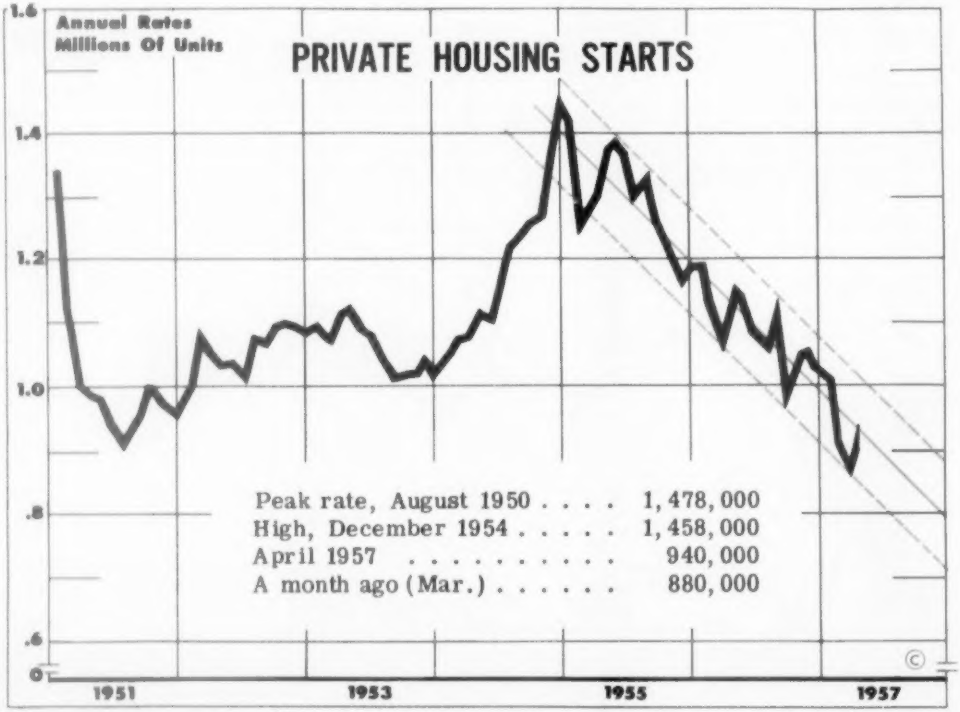
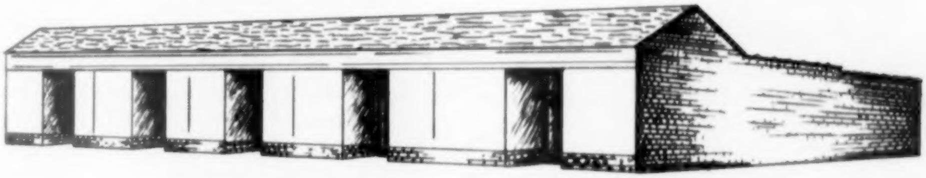


INCREASES IN BUILDING COSTS SINCE 1939

ST. LOUIS
May 1957



COMMERCIAL BUILDING - NO BASEMENT
Content: 115,850 cubic feet
8,075 square feet
Cost 1939: $22,726
(19.6¢ per cubic foot; $2.82 per square foot)
Cost today: $67,680
(58.4¢ per cubic foot; $8.38 per square foot)
INCREASE OVER 1939 = 197.8%

For plans and specifications see page 74 of the Wenzlick Building Cost Manual.

18-FAMILY BRICK APARTMENT
(FRAME INTERIOR)*
Content: 168,385 cubic feet
13,260 square feet
Cost 1939: $ 60,300
(35.8¢ per cubic foot; $ 4.55 per sq. ft.)
Cost today: $177,324
($1.05 per cubic foot; $13.37 per sq. ft.)
INCREASE OVER 1939 = 194.1%

For plans and specifications see page 60 of the Wenzlick Building Cost Manual.

30-UNIT REINFORCED
CONCRETE APARTMENT*
Content: 303,534 cubic feet
21,372 square feet
Cost 1939: $135,000
(44.5¢ per cubic foot; $ 6.33 per sq. ft.)
Cost today: $382,259
($1.26 per cubic foot; $17.89 per sq. ft.)
INCREASE OVER 1939 = 183.2%

For plans and specifications see page 68 of the Wenzlick Building Cost Manual.

*Costs include full basement

(cont. from page 228)

The index of the selling price of existing housing is of great importance to mortgage lenders. If existing housing continues to hold its value or to increase in value, relatively few properties will get into foreclosure difficulties. Foreclosures increase rapidly when the values of existing properties decline, reducing the equity above the mortgage. A radical decline destroys the equity entirely, and the mortgagor loses his enthusiasm for keeping up his payments if the property is not worth on the market the amount of the mortgage.

The chart on page 227, while it does show the radical drop in real estate activity and in mortgage activity, is rather encouraging in a number of other ways. Residential rents are still rising slightly. Foreclosures are still almost negligible. General business remains relatively high, and the general price level is showing no great change. Certainly, with the exception of real estate activity, there is nothing too alarming in the picture as shown on this chart.

The chart on page 228 shows private housing starts seasonally adjusted and expressed as an annual rate. While the rate of new housing starts increased from 880,000 to 940,000, the increase is not yet great enough to prove that the decline in housing starts has stopped. The red dashed lines on this chart show the upper and lower limits of what could be called a normal range in fluctuations. Until the number of starts penetrates the top dashed line, an increase in the rate is not a firm indication that the trend has changed.

The construction cost figures on the preceding page show practically no variation from the figures published in February. The reinforced concrete apartment is down a trifle. The other two buildings are up by microscopic amounts.

The standard six-room frame residence, the cost trend of which is shown at the top of page 227, dropped $11 during the month. This, of course, is insignificant on an item of approximately $18,000.